

The Treasury

Project Korimako - Release of advice

December 2022

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- [33] 9(2)(f)(iv) - to maintain the current constitutional conventions protecting the confidentiality of advice tendered by ministers and officials
- [34] 9(2)(g)(i) - to maintain the effective conduct of public affairs through the free and frank expression of opinions
- [35] 9(2)(g)(ii) - to maintain the effective conduct of public affairs through protecting ministers, members of government organisations, officers and employees from improper pressure or harassment;
- [36] 9(2)(h) - to maintain legal professional privilege
- [37] 9(2)(i) - to enable the Crown to carry out commercial activities without disadvantage or prejudice
- [38] 9(2)(j) - to enable the Crown to negotiate without disadvantage or prejudice
- [39] 9(2)(k) - to prevent the disclosure of official information for improper gain or improper advantage

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Treasury Report: Kiwi Group Holdings: Engagement and Project Initiation

Date:	20 January 2021	Report No:	T2020/3571
		File Number:	SE-2-12-4

Action sought

	Action sought	Deadline
Minister of Finance (Hon Grant Robertson)	Agree to the proposed approach in this report to support Ministers through a negotiating phase and potential transaction(s) in respect of Kiwi Group Holdings Limited during 2021 Indicate your preferences regarding ownership options to be further explored	5 February 2021
Associate Minister of Finance (Hon Dr Megan Woods)	Note the contents of this report	5 February 2021
Associate Minister of Finance (Hon David Parker)	Note the contents of this report	5 February 2021
Minister for State Owned Enterprises (Hon Dr David Clark)	Note the contents of this report	5 February 2021

Contact for telephone discussion (if required)

Name	Position	Telephone	1st Contact
Madeleine Lock	Senior Analyst, Commercial Performance	[39]	[35] ✓
David Stanley	Principal Advisor, Commercial Performance		
Lars Piepke	Principal Advisor, Commercial Performance		

Minister's Office actions

<p>Minister of Finance's office: If the Minister agrees, facilitate the arrangement of separate meetings between the Minister of Finance and the Chairs of New Zealand Post Limited, the Guardians of the New Zealand Superannuation Fund and the Accident Compensation Corporation</p> <p>All offices: Return the signed report to the Treasury</p>

Note any feedback on the quality of the report

Enclosure: No

Executive Summary

This report provides an update on what we understand to be the current strategic positions of the shareholders of Kiwi Group Holdings Limited (KGH), being New Zealand Post Limited (NZ Post) (with a 53% stake in KGH), the New Zealand Superannuation Fund (NZSF) (25%) and the Accident Compensation Corporation (ACC) (22%).

Since the last Treasury advice regarding KGH ownership matters (provided in March 2020), NZ Post and NZSF have communicated their respective positions to the Minister of Finance regarding their ownership intentions for KGH. NZ Post's intention is to divest its stake at the earliest possible opportunity, while NZSF has proposed exploring the possibility of taking a controlling stake in KGH by acquiring NZ Post's shareholding [33]

The agreements which brought the ACC and NZSF in as shareholders of KGH alongside former 100% owner, NZ Post, on 31 October 2016, have a contractual "lock-up" period to 31 October 2021. During this five-year period, only ACC, NZSF and NZ Post can buy or sell KGH shares,¹ but the options to sell outside of the current shareholding arrangement open up after this period. NZSF and NZ Post may have been prompted to state their positions as the lock-up period is nearing its end.

Further, we understand that the differences in each shareholder's risk appetite and preferred investment time frame appear to have increased significantly. [25] and [37]

Based on these observations, we understand the view of the KGH shareholders is that the current ownership arrangements for KGH are sub-optimal [25] and [37]

In light of the stated shareholder positions, the five year contractual lock-up period nearing its end, and the current sub-optimal ownership arrangements, **we recommend that you** undertake the following actions in the first half of 2021:

- 1 **Meet** separately (without officials)² **with the Chairs of NZ Post, NZSF and ACC** as soon as possible, to seek to better understand their strategic positions and preferences, as well as to progress discussions with NZ Post and NZSF in regard to their stated positions.³ We understand that NZSF intends to provide you with a briefing in early 2021 detailing further information on its proposal for KGH – the receipt of any such briefing may further inform the meeting with the Chair of NZSF. We can provide you with suggested talking points for your meetings with the Chairs, if you agree to seek meetings with them.
- 2 **Determine the Government's preferences for KGH ownership**, through exploring the merits and implications of a wider set of viable options for ownership arrangements.

¹ Unless all the KGH shareholders and the Crown were to agree to an alternative arrangement.

² We consider it more likely that each shareholder will be more forthcoming about their preferences and current strategic positioning if you meet separately and without officials with each of the Chairs.

³ For each of ACC and NZSF, it may be appropriate to ensure continuity for Chair successors by inviting the financial institution's Head of Investment Committee Chairs of their respective investment sub-committees, and/or their Chief Investment Officers to the proposed Ministerial meetings regarding KGH matters.

- 3 **Determine the negotiating position of the Crown** to reflect the Government's objectives and preferences for KGH. Negotiations have already effectively commenced, with NZSF and NZ Post having stated their positions, and may lead to a share transaction (or transactions) potentially within the next 12 months.

A number of options for ownership arrangements of KGH are set out at a high-level in this report. If you agree, the Treasury will support you in undertaking the above actions by providing advice to explore the merits and implications of the full range of viable ownership options (or a subset of this), including NZSF's proposal. The advice would provide an analysis of the likely key outcomes for the ownership arrangements under each option, including:

- 1 the extent to which those arrangements might achieve various government objectives (and alternative ways of achieving those objectives, where possible),
- 2 indicative net costs to the Crown of any changes to KGH ownership, and
- 3 timing indications for each option.

In the meantime, if you agree with the proposed approach, **we are also seeking feedback from you on whether there are any options that you would like to, or do not wish to, further explore and whether there are any factors or key decision-making criteria that will influence your decisions.**

Due to the commercially sensitive nature of this project, the establishment of a separate project for any negotiations regarding KGH ownership changes will assist in managing the confidentiality of information flows and the separation of roles.⁴ If you agree to proceed with the proposed approach, this would initiate "Project Korimako." The project team (comprised of Treasury officials and supported by external banking and legal expertise, where required) would provide advice to support the Government's interests in KGH ownership and any potential transaction/s involving KGH shares. We envisage this work programme would commence as soon as possible and continue at least through the first half of 2021.

As agreed with you, this advice is being provided as a work-stream within the Finance portfolio, and copied to Associate Finance Ministers and the Minister for State Owned Enterprises for their information.

⁴ Commercial sensitivities around information flows and role separation are also important in light of insider trading regulations as both Kiwibank and NZ Post have listed market securities.

Recommended Action

We recommend that you:

- a **agree** with the proposed approach to support Ministers through a negotiating phase and potential transaction(s) in respect of Kiwi Group Holdings Limited (KGH), by undertaking the following actions in the first half of 2021:
 - i meet separately with the Chairs of the three shareholders of KGH at the earliest possible opportunity,
 - ii determine the Government's preferences for KGH ownership, through exploring the merits and implications of a wider set of viable options for ownership arrangements, and
 - iii determine the negotiating position of the Crown to reflect the Government's objectives and preferences for KGH.

Agree/disagree.

Minister of Finance

- b **indicate** whether there are any:
 - i options for KGH ownership arrangements in particular that you would like to further explore (regardless of whether those options are included in this report),
 - ii options set out in this report that you do not wish to consider, and/or
 - iii prominent factors or key decision-making criteria that will influence your decisions regarding KGH ownership.

Agree/disagree.

Minister of Finance

Lars Piepke
Principal Advisor, Commercial Performance

Hon Grant Robertson
Minister of Finance

Hon Dr Megan Woods
Associate Minister of Finance

Hon David Parker
Associate Minister of Finance

Hon Dr David Clark
Minister for State Owned Enterprises

Treasury Report: Kiwi Group Holdings: Engagement and Project Initiation

Purpose of report

1. The purpose of this report is to:
 - a provide an update on what we understand to be the current strategic positions of the three shareholders of Kiwi Group Holdings Limited (KGH),
 - b set out a number of high-level options for the future ownership of KGH, and
 - c seek to confirm certain actions and decisions to be made by Ministers in the first half of 2021 with support from the Treasury (which would initiate “Project Korimako”).

Background and context

This advice initiates formal engagement on KGH ownership matters

2. KGH, the parent holding company of Kiwibank Limited (Kiwibank), is currently owned 53% by New Zealand Post Limited (NZ Post), 25% by the New Zealand Superannuation Fund (NZSF) and 22% by the Accident Compensation Corporation (ACC).
3. The agreements which brought ACC and NZSF in as shareholders of KGH alongside former 100% owner, NZ Post, on 31 October 2016, have a contractual “lock-up” period to 31 October 2021. As provided for in the Crown Deed,⁵ during this five-year period, only ACC, NZSF and NZ Post can buy or sell KGH shares (unless all the KGH shareholders and the Crown were to agree to an alternative arrangement).
4. The Crown Deed provides that after 31 October 2021 the three existing KGH shareholders continue to have priority over any share transactions, however, any KGH shares available for transfer from NZSF and ACC that are not acquired by the other KGH shareholders can be offered to the Crown. As long as certain other requirements are met, this is also the case for NZ Post’s shares. Shares offered but not taken up by other existing KGH shareholders or the Crown may be offered to third parties (although in the case of NZ Post’s shares this would require the prior written consent of the Crown).
5. However, the Crown has effective control over whether all KGH shares remain owned (indirectly or directly) by the Crown. The Crown Deed has a number of provisions ensuring that the Crown can buy any shares which might otherwise be intended for sale to a third party (i.e. a transaction involving third parties can only take place with Crown consent or if the Crown does not exercise its purchase rights). There are also certain circumstances under which existing KGH shareholders can require the Crown to acquire their shares.⁶

⁵ The Crown Deed is one of the four legal documents related to the sale of 47% of KGH from NZ Post to ACC and NZSF on 31 October 2016 (Project Tui) and binds the Crown, ACC, NZ Post and NZSF.

⁶ [25]

6. With the lock-up period now having less than a year to go, we are seeking to re-engage with you on your preferences in relation to KGH on the basis that:
 - a changes to the current ownership arrangements are likely to be necessary in order to maximise the value of KGH's operating subsidiaries, and
 - b we understand that the current KGH shareholders are actively considering their strategic ownership options in light of the lock-up period nearing its end.

This advice is being provided as a work-stream in the Finance portfolio

7. The considerations for the Government regarding ownership of KGH go beyond the individual shareholding responsibilities of NZ Post, or Ministerial responsibilities regarding NZSF or ACC. The objectives of the current shareholders will be to maximise their respective returns through either further investment in, or exit from, KGH ownership. You may have wider objectives, including how bank ownership might enable (or otherwise impact on) the Government's objectives for the banking sector.
8. As agreed with you, this advice is therefore being provided as a work-stream within the Finance portfolio, and copied to the Associate Ministers of Finance and the Minister for State Owned Enterprises for their information.

Strategic positioning of the KGH shareholders

The current KGH ownership settings are sub-optimal

9. [25] and [26]

In addition, the differences in each shareholder's risk appetite and preferred investment time frame appears to have increased significantly. [25] and [37]

10. [25]

At least two of the three KGH shareholders are seeking new ownership arrangements

11. The Chair of NZ Post has stated his board's position regarding NZ Post's ownership of KGH (in a meeting with Ministers on 20 February 2020 and as indicated in his letter to the incoming Minister for State Owned Enterprises of 6 November 2020). The Board's position is that NZ Post no longer has a compelling strategic rationale for its investment in KGH and the company intends to divest its stake in KGH at the earliest possible opportunity.

12. NZSF clearly stated its position in its briefing to the incoming Minister of Finance in November 2020. NZSF proposed to explore the option of taking a controlling stake in KGH by acquiring NZ Post's shareholding (which would bring its total shareholding to 78%). [33]

[26]

and, "*put Kiwibank and Kiwi Wealth on accelerated growth and transformation trajectories.*"

13. ACC is yet to formally advise Ministers of its current strategic positioning regarding KGH. However, as ACC and NZSF are Crown-owned institutional investors, their objectives are to make investments that meet their respective investment criteria. [25], [26]

14. [34]

15. Whatever approach the KGH shareholders may prefer to undertake will depend on each of their current strategic objectives and the extent to which commercially satisfactory terms can be reached between the KGH shareholders, consistent with the existing KGH Shareholder Agreement and Crown Deed (or outside those arrangements if the terms could be agreed between the KGH shareholders and the Crown).

The Government is entering a negotiating period on ownership changes for KGH

16. In our view, the Government has now entered a phase where there could be substantive negotiations with the three shareholders of KGH regarding future ownership arrangements for the holding company (and its operating subsidiaries). While all three shareholders engage with the Crown under the "no surprises" convention and the Crown Deed requires that they will keep the Crown informed of their intentions in respect of the ownership of KGH, there is no requirement for them to reveal all the elements of any strategies they may have for potential negotiations with the Crown.
17. Further, each of the KGH shareholders' directors and the directors of KGH itself have an obligation to act in what they believe to be the best interests of the entities that they govern (under the Companies Act 1993) and should therefore prioritise this obligation ahead of the Government's or individual shareholder's objectives for KGH (which may be different).
18. Factors that further drive the timing imperative for Ministers to engage on KGH ownership matters as soon as possible include that:
- a it is possible that the KGH shareholders could explore offering shares to third parties sometime in 2021 (with intended effect after 31 October 2021),

⁷ [33]

- b developing a Crown strategy in relation to the ownership of KGH will take some time [33] and
 - c public speculation regarding KGH ownership may emerge nearer the end of the lock-up period.
19. You may therefore wish to determine ownership preferences for KGH on behalf of the Government and establish a strategy for engaging with the KGH shareholders during the first half of 2021.

Government may be better informed by initially seeking separate engagements with Chairs

20. The KGH shareholders have responsibilities to each other as agreed under the KGH Shareholders Agreement and to their own boards to act in a manner consistent with their own organisational objectives. Therefore NZ Post, NZSF and ACC may be hesitant to fully communicate their own organisation's strategic planning externally (especially in a broader meeting environment). We consider it more likely that each shareholder is likely to be more forthcoming about their preferences and current strategic positioning if you meet separately (and without officials) with each of the Chairs of NZ Post, NZSF and ACC.⁸
21. **We recommend that the Minister of Finance requests to meet separately with the Chairs of NZ Post, NZSF and ACC at the earliest possible opportunity.** This will enable the Government to be better informed to consider its options regarding KGH, progress discussions with NZ Post and NZSF in regard to their stated positions, and to seek to understand the position of ACC.
22. We can provide you with suggested talking points for your meetings with the Chairs of the three KGH shareholders, if you agree to seek meetings with them.

Retention of NZ Post's shareholding in the meantime will maintain a wider option set

23. NZ Post has signalled a desire to further sell-down its shareholding within the lock-up period. The current shareholders can transfer shares of KGH within their shareholding group at any time, without the consent of the Crown (subject to the controlling interest limitation in respect of NZSF and where shareholder approval is required for major transactions⁹ in respect of NZ Post).
24. However, as NZ Post is a State Owned Enterprise, its 53% shareholding in KGH is still the Crown's best lever for maintaining influence over the future ownership arrangements for KGH. Therefore, the most recent two Letters of Expectations (LOEs) from shareholding Ministers to NZ Post (covering the 2019/20 and 2020/21 financial years) have included an expectation that NZ Post preserves its shareholding in KGH until the Government has determined its preferences for KGH. We have recommended in the proposed LOE for 2021/22 (*T2020/3541 refers*) that this expectation is maintained; however, noting that Ministers expect to communicate their preferences for NZ Post's stake in KGH to the Board of NZ Post in the first half of 2021.

⁸ For each of ACC and NZSF, it may be appropriate to ensure continuity for Chair successors by inviting the financial institution's Head of Investment Committee Chairs of their respective investment sub-committees, and/or their Chief Investment Officers to the proposed Ministerial meetings regarding KGH matters.

⁹ Shareholder approval is required if the value of a transaction meets the threshold for a "major transaction", being at least 50% of the company's total asset value, per the Companies Act 1993. The total value of KGH in NZ Post's 2019/20 financial statements is 49% of its total reported asset value.

Options for the future ownership of KGH

Other options for the ownership of KGH may be viable in addition to NZSF's current proposal

25. The investment objectives of NZSF are determined independently from those of the Government, as an arm's length institutional investor. [34]

26. You may wish to determine whether your objectives are sufficiently aligned to NZSF's investment objectives. Where you have wider or different objectives, there are a number of alternative options that you may wish to explore further, in addition to NZSF's current proposal.

Preferred ownership arrangements depend on the Government's objectives

27. The Government's preferred ownership arrangement for KGH will depend on your objectives for the banking sector and how those objectives might be achieved through bank ownership, or through other arrangements. For example, your objectives could include: keeping a portion of banking sector profits in New Zealand; retaining ownership of a significant competitor bank in New Zealand; [25]

28. [25]

You may be able to achieve some of your objectives through bank ownership, while others may be more effectively achieved outside it, e.g. through regulation or contract.

Other ownership options and how these align to government objectives can be explored

29. While the Government's objectives are yet to be fully determined, we consider it likely to be most beneficial to explore a wide range of options for the future ownership of KGH. We expect that through considering wider ownership options, you will be able to further determine and clarify your policy objectives relating to the banking sector and KGH. This will inform a pathway of work to establish the Government's strategic position vis-à-vis the positions that have been communicated by NZ Post and NZSF, and any others that emerge in coming months. We envisage this work programme will commence as soon as possible and continue through the first half of 2021.

30. Viable ownership arrangements may involve partial or full, indirect or direct, ownership of KGH. **Table 1** (on the next page) provides possible high-level options around future ownership arrangements for KGH for your initial consideration. If you agree to receive further advice, we can provide an analysis on the likely key outcomes for the ownership arrangements under each option, including:

- a the extent to which those arrangements might achieve various government objectives (and alternative ways of achieving those objectives, where possible),
- b indicative net costs to the Crown of any changes to KGH ownership, and

- c timing indications for each option.
31. We have not included the following options within Table 1, so as to simplify the initial option set being conveyed through this report:
- a [34]
 - b [25]

Table 1: High-Level Options for KGH Ownership

		Ownership proximity to Crown	
		Direct	Indirect
Crown Ownership Share	Full	Options set 1	Options set 2
		a Crown holds 100% of KGH directly	<ul style="list-style-type: none"> a NZSF holds 100% of KGH; b Another Crown-owned entity holds 100% of KGH; c NZSF (or another Crown-owned entity) holds almost 100%, with a Crown “Kiwi Share”; or d Crown owns part directly and part through a Crown-owned entity, i.e.: <ul style="list-style-type: none"> i. Crown / NZSF joint venture (JV); or ii. Crown / other Crown-owned entity JV
	Partial	Options set 3	Options set 4
		<ul style="list-style-type: none"> a Crown / private investor JV; or b Mixed ownership model (MOM) with partial direct Crown ownership (partially listed on the New Zealand Stock Exchange (NZX)). 	<ul style="list-style-type: none"> a JV between a private investor and: <ul style="list-style-type: none"> i. NZSF; or ii. Other Crown-owned entity; or b MOM with partial indirect Crown ownership via: <ul style="list-style-type: none"> i. NZSF; or ii. Other Crown-owned entity

You may wish to consider your key decision criteria as part of further advice commissioned

32. Key factors that may influence your decisions on the high-level options in Table 1 above include (but are not limited to):
- a The degree of influence that the Government wants to retain over future ownership of KGH and its subsidiaries:
 - i For example, you may wish to explore other options if you do not consider that the ownership of KGH via a controlling interest held by NZSF would enable the achievement of your wider objectives. As an institutional investor, NZSF only invests where there are also clear mechanisms for it to be able to exit the investment sometime in the future. While NZSF may hold investments for a very long time period if they continue to meet its investment criteria, there is always the possibility that it moves to monetise all or part of any existing investment in order to redeploy funds elsewhere.

- b The cost of any changes to ownership:
- i Funding sensitivity will be important for you to establish in terms of movements of cash between the Crown and its entities, recovery and other uses of capital, and the impact of timing on the cost to the Crown.
 - ii We recognise that any transactions between the current shareholders will reflect transfers of funding around different parts of the Crown and central Government. However, as you consider the magnitude of alternative demands for Crown funding, the ability for funds to be returned to the centre may (or may not be) a key factor in your decision-making.
- c The nature and extent of governance arrangements that would be appropriate where ownership is retained (partially or fully) within the Crown:
- i [25]
 - ii If another Crown-owned entity were to be brought into the shareholding arrangements (either to wholly-own KGH, or partially own KGH in a joint venture with the Crown or with NZSF), you may wish to establish key criteria for that entity. For example, an existing or new entity that has:
 - clear institutional arrangements,
 - involves directors with a good track record of strong governance in relevant sectors, and
 - sound investment management practices.
- d Other wider market objectives the Government may seek to achieve through direct or indirect, partial or full, ownership of KGH (beyond the banking sector), such as for example, outcomes for New Zealand's capital markets by being listed on the NZX (the approach that has been used for Air New Zealand Limited and the partially Crown-owned energy companies).

Please indicate whether you would like to further explore options and/or objectives

33. If you agree with the proposed approach, the Treasury will support you in determining the Crown's objectives, and negotiating position, regarding the ownership of KGH by providing advice to explore the merits and implications of a range of viable ownership options, including NZSF's proposal. As a next step, we intend on engaging specific external expertise¹⁰ in order to canvass the implications and viability of the options set out in Table 1 (or a subset of these).
34. We **recommend** that you indicate whether there are any:
- a options for KGH ownership arrangements in particular that you would like to further explore (regardless of whether those options are included in this report),

¹⁰ For example, the legal firm that advised the Treasury in relation to the negotiations that introduced ACC and NZSF as shareholders of KGH (Project Tui) would likely be well placed to assist with the advice on aspects of the various options.

- b options set out in this report that you do not wish to consider, and/or
- c prominent factors or key decision-making criteria that will influence your decisions regarding KGH ownership.

Project Korimako initiation

- 35. If you agree to proceed with the proposed approach and engage on a programme of work regarding a wider set of ownership arrangements for KGH (including NZSF's proposal) then in our view this would be best achieved through the initiation of a new project, given the commercially sensitive nature of this work. The project will potentially result in a KGH ownership transaction within the next 12 months, pursuant to your preferred arrangement (subject to negotiations with the current KGH shareholders). We suggest this project be known as Project Korimako.
- 36. As discussions between parties advance, there will be an accentuation of differences in the responsibilities and interests of the parties which will, in turn, have implications for Ministers involved directly or indirectly in those negotiations and all of which will need to be carefully managed. The Minister of Finance, for example, has roles in relation to banking sector oversight, is the Responsible Minister for ACC and NZSF, is a shareholding Minister for NZ Post and is part of the Crown. Acting on behalf of the Crown, Ministers could enter into direct negotiations with the shareholders of KGH if the Crown seeks to own all or part of KGH directly, and/or in regards to the arrangements under the Crown Deed regarding future exit arrangements for any Crown-owned organisations continuing as shareholders. Similar issues exist for Crown officials (in particular, within the Treasury) and any professional advisors engaged by the Crown and KGH shareholders collectively and individually.
- 37. Managing these issues will require both information-flow management as well as some separation and/or delegation of specific responsibilities in relation to any potential transaction negotiations. The advice we prepare will include recommendations on managing those various roles and information flows as discussions advance and evolve into formal negotiations (in whatever form these negotiations might take).
- 38. The project team would consist of Treasury advisors from its Commercial Performance team, with consultation from its Financial Markets, Financial Institutions and Legal teams. The Project Team will take direction from Ministers and act as lead negotiators on behalf of the Crown (possibly outsourcing the commercial advisor role to an external party). External advisors and external legal assistance will be engaged, as needed.

Next steps

- 39. If you agree, you may wish to **instruct** your office staff to **facilitate separate meetings** with the three Chairs of NZ Post, NZSF and ACC (and any senior personnel or other directors from those entities that the Chairs may identify as required) regarding their intentions and preferences for KGH ownership (to take place as soon as possible in 2021). We consider that one-on-one meetings between you and each Chair (i.e. without officials) will result in gathering the most (although by no means complete) insight into individual shareholder strategies and intentions. We can provide suggested talking points for those meetings.
- 40. Subject to your agreement with the proposed approach in this report, the Treasury will provide further advice regarding options for any future KGH ownership arrangements that you would like to explore.